(8)

No. 95-325

In the Supreme Court of the United States

OCTOBER TERM, 1995

UNITED STATES OF AMERICA, PETITIONER

v.

REORGANIZED CF&I FABRICATORS OF UTAH, INC., COLORADO & UTAH LAND COMPANY, KANSAS METALSCOMPANY, ALBUQUERQUE METALS COMPANY, REORGANIZED PUEBLO METALS COMPANY, DENVER METALS COMPANY, REORGANIZED PUEBLO RAILROAD SERVICE COMPANY, REORGANIZED CF&I FABRICATORS OF COLORADO, INC., REORGANIZED CF&I STEEL CORPORATION, AND REORGANIZED COLORADO AND WYOMING RAILWAY COMPANY

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE TENTH CIRCUIT

REPLY BRIEF FOR THE UNITED STATES

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1. The first question presented in this case is whether a claim for the excise tax imposed under Section 4971(a) of the Internal Revenue Code is entitled to the priority granted to "an excise tax" under Section 507(a)(7)(E) of the Bankruptcy Code, 11 U.S.C. 507(a)(7)(E)(1988).

a. Excise taxes are frequently imposed by Congress with the principal purpose of deterring undesired conduct rather than simply raising revenue. Section 4971 is one of the substantial number of federal excise taxes that have a deterrent purpose (Pet. Br. 15-17). The excise tax imposed by Section 4971(a) is designed to insure prompt compliance with the funding obligations of qualified pension plans (Pet. Br. 14).

The priority that Congress afforded to this excise tax in Section 507(a)(7)(E) of the Bankruptcy Code has "an extremely beneficial effect on pension funding" by ensuring that employers—and competing creditors who can force an involuntary reorganization of the employer—cannot evade pension obligations by commencing a bankruptcy case (Amicus PBGC Br. at 2). For example, respondents state that a significant reason for their bankruptcy filing was the accrual of unpaid pension funding obligations (Resp. Br. 3). If creditors could, by forcing an employer into bankruptcy and obtaining a liquidation of its assets, reduce the portion of those assets to be paid in satisfaction of outstanding pension funding obligations, the creditors would thereby benefit at the expense of plan participants and the pension benefit guaranty system of the United States. The bankruptcy priority afforded to the Section 4971(a) excise tax reduces the financial incentives that employers, and their creditors, would otherwise have to evade the timely funding of pension obligations.[1]

[1] Respondents claim that it was "incongruous" for Congress to grant priority to the excise tax imposed by Section 4971(a) over the claims of the PBGC or of the direct beneficiaries of the plan (Resp. Br. 28; see also United Steel Workers Amicus

b. In enacting the Bankruptcy Code in 1978 and granting a specific priority to excise taxes for the first time, Congress did not distinguish among excise taxes based on their purpose.[2] Instead, the unqualified text of Section 507(a)(7)(E) reflects what its history clearly states: the statutory priority for "excise taxes" extends to any "Federal, State or local taxes generally considered or expressly treated as excises." 124 Cong. Rec. 32,416 (1978) (Rep. Edwards). See Pet. Br. 13.

Br. at 14). That contention improperly focuses solely on the consequences of the priority for a particular plan. Respondents fail to recognize that, by diminishing the economic incentive that otherwise exists for an employer to refuse to make plan payments in anticipation of a bankruptcy filing, the priority provided for the Section 4971(a) excise tax seeks to insure the full and timely funding of *all* pension plans in *advance* of bankruptcy. See H.R. Rep. No. 807, 93d Cong., 2d Sess. 28 (1974).

[2] By contrast, as we have noted, in providing a limited priority for prepetition "penalties" in Section 507(a)(7)(G), Congress *did* distinguish among such claims based on whether or not their "purpose" was to compensate the government for a "pecuniary loss." See 11 U.S.C. 507(a)(7)(G); Pet. Br. 17-18. If Congress had intended, as respondents contend, to exclude from the priority for "excise taxes" in Section 507(a)(7)(E) any excise tax that might be "punitive" rather than "compensatory" in nature, it had to look no further than Section 507(a)(7)(G) for a model.

As discussed in our opening brief (Pet. Br. 17-18 n.10), an excise tax granted priority under Section 507(a)(7)(E) need not *also* fit within the priority granted in Section 507(a)(7)(G) to penalties "related to a [priority tax] claim * * * and in compensation for actual pecuniary loss." The courts below erred precisely in concluding that an excise tax that would not qualify for priority under the latter provision also must be denied priority under the former.

Recognizing that "many, if not most of the excise taxes contained in * * * the Internal Revenue Code are intended to discourage undesirable conduct," the Sixth Circuit correctly held in *United States* v. *Mansfield Tire & Rubber Co.*, 942 F.2d 1055, 1058 (1991), cert. denied, 502 U.S. 1092 (1992), that "Congress granted priority to excise tax claims without regard to whether their purpose was primarily regulatory." For the reasons explained in detail in our opening brief (Pet. Br. 13-20), the court of appeals erred in this case by denying priority to the Section 4971(a) excise tax on the ground that it is principally a "penalty" and only secondarily designed to raise revenue.

c. Respondents devote a large portion of their brief (Resp. Br. 14-29) to the proposition that, under the case law developed under the pre-1978 Bankruptcy Act, the tax imposed by Section 4971 is more like a "penalty" than a "tax." That issue might have had relevance under the former Bankruptcy Act, which distinguished between "taxes" and "penalties" and had no specific priority for "excise taxes." But it is not relevant in deciding the proper scope of the specific, new priority that Congress provided in 1978 for "excise taxes," which are commonly "punitive" or "deterrent" in nature. See Pet. Br. 16. Instead, Congress indicated that the priority for "excise taxes" applies to all exactions "expressly treated" or "generally considered" as excises. 124 Cong. Rec. at 32,416. See also note 1, *supra*.

Moreover, the pre-1978 decisions of this Court on which respondents seek to rely (Resp. Br. 16-19) do not purport to distinguish "excise taxes" from penalties. Two of the three decisions that respondents cite dealt with the question whether a particular state exaction was a "tax" within the former provisions of the Bankruptcy Act. *City of New York* v. *Feiring*, 313 U.S. 283 (1941); *New Jersey* v. *Anderson*, 203 U.S. 483 (1906). The third decision concerned whether an employer's responsibility to remit withheld federal taxes owed by employees was a priority "tax" or an unsecured "debt," as the employer contended. *United States* v. *New York*, 315 U.S. 510, 513 (1942).

Contrary to respondents' contention (Resp. Br. 18), the Court in *United States* v. *New York* did not suggest that it is appropriate to look behind the "label" that Congress employs in designating what is a "tax" and what is a "penalty" for purposes of the priorities that then applied under the Bankruptcy Act. To the contrary, the Court suggested only that an exaction that Congress had *not* specifically labelled as a "tax" could nonetheless qualify as a "tax" under the Bankruptcy Act if it possessed characteristics that generally indicated it to be a tax. See 315 U.S. at 515.[3] In providing the new, specific priority for "excise taxes" under the Bankruptcy Code, Congress expressed a consistent intention—that any exaction that it had "expressly treated" as an excise tax *or* that was "generally considered" to be an excise tax would be entitled to priority. 124 Cong.

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[3] In *United States* v. *New York*, the Court cited *City of New York* v. *Feiring*, *supra*, for the proposition that the duty to pay over a withheld tax is itself the duty to pay a "tax" for purposes of the then-applicable priority provisions of the Bankruptcy Act. 315 U.S. at 515. The Court also rejected the suggestion that related tax credit provisions represented a "penalty." See *id.* at 516-517. In doing so, however, the Court did not cite or refer to *City of New York* v. *Feiring*, as respondents erroneously imply (Resp. Br. 18-19).

Rec. at 32,416 (Rep. Edwards); *id.* at 34,016 (Sen. DeConcini).[4]

As the court stated in *United States* v. *Mansfield Tire & Rubber Co.*, 942 F.2d at 1060, Congress did not intend "to have its *own* characterizations of payments as 'taxes' subject to second-guessing by the federal courts." See *id.* at 1059:

> While a federal court may ultimately be called upon to decide the question where a state or local exaction is at issue, in this case we are concerned with a federal excise tax. Where Congress has exercised its constitutitonal power and deemed an exaction an "excise tax," the question has been answered.

d. Respondents nonetheless claim that the legislative history of Section 507(a)(7)(E) of the Bankruptcy Code reflects that the statutory priority extends only to "traditional, transaction-based excise taxes" rather than to "penalties" (Resp. Br. 29-30) and does not reach excise taxes "imposed only upon violation of a statute" (Resp. Br. 39). They base this proposition exclusively on the portion of the legislative history that lists, as examples of excise taxes, "sales taxes, estate and gift taxes, gasoline and

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[4] The reasoning of this Court's pre-1978 decisions under the Bankruptcy Act remains relevant under the Bankruptcy Code in classifying exactions that are not designated as "taxes" (see *United States* v. *River Coal Co.*, 748 F.2d 1103 (6th Cir. 1984); *LTV Steel Co.* v. *Shalala* (*In re Chateaugay Corp.*), 154 B.R. 416 (S.D.N.Y 1993)) and in classifying exactions of state or local governments (see *Ohio Bureau of Workers' Compensation* v. *Yoder*, 36 F.3d 484 (6th Cir. 1994); *In re Payne*, 27 B.R. 809 (Bankr. D. Kan. 1983)).

special fuel taxes, and wagering and truck taxes" (124 Cong. Rec. at 32,416).

But the examples contained in this non-exclusive list include excise taxes that could be considered to have a "punitive" or "deterrent" purpose. Moreover, at least one of these excise taxes is "imposed only upon violation of a statute." For example, the "wagering" tax is imposed under Section 4401 of the Internal Revenue Code on persons engaged in the business of accepting wagers and is levied at two different rates. For "any wager authorized under the law of the State in which accepted," the excise tax is 0.25 percent of the wager; for wagers that are not authorized under state law, the excise tax is eight times higher—2.00 percent of the wager. 26 U.S.C. 4401(a). The significantly higher rate of the excise tax for unauthorized wagers is obviously designed to discourage and deter unlawful behavior. The inclusion in the legislative history of Section 507(a)(7)(E) of "wagering" taxes as an example of excise taxes that fall within the scope of the statutory priority indicates, as the plain language of the statute reflects, that Congress did not intend to deny priority to any federal excise tax simply because it has a "punitive" or "deterrent" purpose. See also Pet. Br. 16 (listing examples of federal excise taxes, such as the excise tax on unlawfully issued securities (26 U.S.C. 4701) and the excise tax on excess lobbying by public charities (26 U.S.C. 4911)); note 1, *supra*.

Nor are respondents correct in their assertion (Resp. Br. 33-34) that the excise tax imposed by Section 4971(a) is not within the statutory priority because it is not imposed on a "transaction." Section 507(a)(7)(E) provides priority to "an excise tax on * * * a transaction occurring before the date of the

filing of the petition" (11 U.S.C. 507(a)(7)(E)(i)). Even though Congress unquestionably intended this excise tax priority to have a broad scope (see page 3, *supra*), respondents claim that the term "transaction" should be narrowly construed and does not include the "act of maintaining a pension plan that is not funded adequately" (Resp. Br. 34).

The ordinary definition of "transaction" contradicts respondents' contention. The word has a broad and flexible meaning; it refers (*Black's Law Dictionary* 1668 (4th ed. 1968) (emphasis added)) to an:

> [a]ct of transacting or conducting any business; negotiation; management; proceeding; that which is done; an affair. * * * Something which has taken place, whereby a cause of action has arisen. It must therefore consist of *an act* or agreement, *or several acts* or agreements having some connection with each other, *in which more than one person is concerned, and by which the legal relations of such persons between themselves are altered.*

The "act of maintaining a pension plan that is not funded adequately" fits squarely within this standard definition of the word "transaction"—a definition that respondents adopt and concede is applicable here (Resp. Br. 34). In *United States* v. *Mansfield Tire & Rubber Co.*, 942 F.2d at 1059 n.4, the Sixth Circuit therefore correctly rejected respondents' claim that the excise tax under Section 4971(a) is not imposed on a "transaction" within the meaning of Section

507(a)(7)(E). No other court has ruled to the contrary.[5]

e. Respondents err in stating that it is the government's position that "*every* substantive term used in the Internal Revenue Code must have an identical meaning when used in the Bankruptcy Code, as well as in every other federal statute" (Resp. Br. 24). Our submission does not advance that broad proposition.

This case concerns only whether, by enacting a statutory priority for "excise taxes" in Section 507(a)(7)(E) of the Bankruptcy Code, Congress created a priority that encompasses the excise tax imposed by Section 4971(a) of the Internal Revenue Code. It would, indeed, have been odd for Congress to have referred specifically to the Internal Revenue Code in describing the "excise tax" priority in Section 507(a)(7)(E), for the statute provides priority not only for federal excises but for state and local excises as well. Congress, however, *did* express its understanding that the taxes that it has "expressly treated" as excises, as well as other exactions "generally considered" to be excises, are encompassed within the priority for "excise taxes" created by Section 507(a)(7)(E). See 124 Cong. Rec. at 32,416 ("All Federal, State or local taxes generally considered or expressly treated as excises are covered by this category."). See also note 2 *supra*.

f. Respondents attempt to inject a far different set of questions into this case than are in fact presented. They contend that, if the ten percent excise tax on late funding of pension obligations under Section

[5] Respondent did not raise this contention in the bankruptcy or district court. When it was raised for the first time in the court of appeals, the court did not address it.

4971(a) qualifies for priority as an "excise tax," then the 100 percent tax that is imposed under Section 4971(b) of the Internal Revenue Code would also be entitled to the same priority. The latter provision imposes a tax of 100 percent of the amount of an unfulfilled funding obligation that has not been corrected by the end of a statutory period that may be extended or waived. 26 U.S.C. 4971(b); see 26 U.S.C. 4961(a), 4963(e)(1)(B). Respondents assert that, if the 100 percent tax for uncorrected funding deficiencies under Section 4971(b) is entitled to priority as an "excise tax," it would be impossible for employers who consistently fail to meet their pension obligations to reorganize in bankruptcy (Resp. Br. 38-39; see also Resp. Br. 9, 12, 27).

The complicated and far-ranging set of issues that respondents thus seek to raise are not presented in this case:

(i) In the first place, the question of what bankruptcy priority would apply to the 100 percent tax for uncorrected funding deficiencies is not presented in this case because it is not raised here. The government's claim for this 100 percent tax was disallowed—not subordinated—by the bankruptcy court, and that ruling was not appealed. The claim was disallowed on the theory that the debtor's failure to cure the funding deficiency occurred *after* the petition was filed, at a time when the court believed respondents to be legally disabled from paying any prepetition debts (Pet. App. 54a).[6] Whether a debtor may legally make pension contributions after the date of the petition in bankruptcy is a controversial issue that is not now before the Court. See note 6, *supra*.[7]

By contrast, the missed contribution that gave rise to the ten percent excise tax under Section 4971(a) that *is* at issue in this case was due *before* the commencement of this bankruptcy case (Resp. Br. 2). Nothing in bankruptcy law prohibited respondents from making that pre-filing contribution on a timely basis. The bankruptcy court therefore properly allowed the Section 4971(a) excise tax claim, and it is the priority of *that* claim that is at issue in this case.

(ii) Respondents' suggestion (Resp. Br. 38-39) that an employer that cannot meet its pension plan obligations could not successfully reorganize fails to take account of the direct relief that is available to such an employer under ERISA. An employer experiencing temporary difficulty in making pension contributions may apply to the Secretary of the Treasury for a waiver of that year's funding obligation upon a showing of "temporary substantial busi-

[6] The district court similarly held that respondents' failure to make postpetition contributions to its underfunded pension plans was excused. *PBGC* v. *Reorganized CF&I Fabricators, Inc.*, 179 B.R. 704, 708 (D. Utah 1994). Other courts, however, have held that funding contributions due during a Chapter 11 reorganization are to be paid as postpetition administrative expenses with a "[f]irst" priority under 11 U.S.C. 507(a)(1). See, *e.g.*, *Columbia Packing Co.* v. *PBGC*, 81 B.R. 205, 209-210 (D. Mass. 1988) (pension contributions are properly viewed as "an ongoing, current cost of labor"); *In re Pacific Far East Line, Inc.*, 713 F.2d 476, 479-480 (9th Cir. 1983) (same under former Bankruptcy Act). If the latter view prevails, postpetition funding contributions may be made in future bankruptcies and the taxes imposed by Section 4971(b) thereby avoided.

[7] Moreover, the "excise tax" priority of Section 507(a)(7)(E) expressly applies only to prepetition excise tax claims (see 11 U.S.C. 507(a)(7)(E)). That priority is thus not applicable in determing the proper treatment of postpetition claims under Section 4971(b) of the Internal Revenue Code.

ness hardship." 26 U.S.C. 412(d)(1). If the difficulty is more than temporary, a debtor may terminate its pension plan in a "distress termination" if it can demonstrate to the bankruptcy court that it will not otherwise be able to reorganize. 29 U.S.C. 1341(c)(2)(B)(ii).[8] If the court approves termination of the plan, the employer's obligation to make future funding contributions is thereby terminated. See Rev. Rul. 79-237, 1979-2 C.B. 190. In this case, it was respondents' inaction that caused its obligation to make pension contributions to continue to accrue long after the bankruptcy case was commenced. Respondents did not take appropriate steps available under ERISA and the Bankruptcy Code to limit their pension liability.[9]

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[8] In fashioning this test, Congress "tried to balance the need to limit access to the [plan termination] insurance system to cases of genuine need against the danger of making the tests so stringent that nothing short of total liquidation would qualify for PBGC assistance." H.R. Rep. No. 241, 99th Cong., 1st Sess., Pt. 2, at 49 (1985).

[9] Respondents seek to excuse this inaction by noting that they asked the PBGC to terminate the plan "unilaterally" (Resp. Br. 3 n.4). The authority of PBGC to terminate a plan is designed "to protect the interests of the participants" and to avoid increases "in the liabiliity of the [PBGC]." 29 U.S.C. 1342(c). That authority is not intended as a mechanism for the debtor to abandon the obligations of its collective bargaining agreement with the employees. If termination of the pension plan was essential to the reorganization but was not permitted under the collective bargaining agreement (see 29 U.S.C. 1341(a)(3)), respondents could have applied to the bankruptcy court under 11 U.S.C. 1113 for relief from the collective bargaining agreement. Respondents complain that such measures are time-consuming (Resp. Br. 39). But the Bankruptcy Code assures an employer a prompt hearing and ruling on an application to reject a collective bargaining agreement. See 11 U.S.C. 1113(d) (requiring the bankruptcy court to schedule a hearing within 14 days after the commencement of the hearing, with only one seven-day extension permitted absent an agreement of the parties).

(iii) Finally, we do not contend that the answer to the question that *is* presented in this case would also resolve whether a prepetition liability for the 100 percent tax imposed under Section 4971(b) is within the "excise tax" priority of Section 507(a)(7)(E) of the Bankruptcy Code. A determination that the ten percent excise tax imposed under Section 4971(a) is entitled to priority under Section 507(a)(7)(E) does not necessarily mean that the 100 percent tax imposed under Section 4971(b) is entitled to the same priority.

There are several distinctions between these two subsections. For example, the Secretary of the Treasury may, in "appropriate cases," waive imposition of the 100 percent tax under Section 4971(b) but has no authority to waive the ten percent tax under Section 4971(a). Employee Retirement Income Security Act of 1974, Pub. L. No. 93-406, 88 Stat., 997, § 3002(b); see 26 U.S.C. 4971(g) (cross reference).[10] The Secretary is also authorized to reduce the employer's funding requirement (26 U.S.C. 412(d)) and then abate the 100 percent tax (26 U.S.C. 4961(a)).[11] Whether

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[10] See also H.R. Conf. Rep. No. 1280, 93d Cong., 2d Sess. 292 (1974) ("[t]he Service will be able to waive (or abate) the second level, but not the first level, tax upon a correction of underfunding that is obtained by the Secretary of Labor").

[11] By contrast, the ten percent excise tax imposed by Section 4971(a) is not subject to abatement even if "reasonable cause" for the failure to pay exists (26 U.S.C. 4962(a)(1)). See Section 4962(b) (making that standard applicable only to taxes imposed under 26 U.S.C. 4940-4948 and 26 U.S.C. 4955).

these and other distinctions between the fixed excise tax imposed under Section 4971(a) and the waivable tax imposed under Section 4971(b) are instrumental in application of the priority established in Section 507(a)(7)(E) of the Bankruptcy Code is an issue that is not presented in this case and that the Court need not address.

2. If the Court agrees that the excise tax imposed by Section 4971(a) is entitled to priority under Section 507(a)(7)(E) of the Bankruptcy Code, the second question presented in this case need not be addressed. Respondents do not contend that, if the government's claim is entitled to a statutory priority, it may then be subordinated under the "principles of equitable subordination" codified in Section 510(c) of the Bankruptcy Code.[12]

a. The second question presented in this case is whether, if the claim for the Section 4971(a) excise tax is *not* entitled to a statutory priority, it may be subordinated to other nonpriority unsecured claims under the "principles of equitable subordination" that Congress codified in Section 510(c) of the Bankruptcy Code. Relying exclusively on "principles of equitable subordination," the courts below approved a plan of reorganization that places the Section 4971(a) excise tax claim in a subordinated class and then further provides that, if the government's claim "should not be subordinated, such Claim shall be treated in [the class for nonsubordinated general unsecured claims]" (CF&I R. 141; see Resp. Br. 11). If the Section 4971(a) claim in this case is *not* entitled to a statutory

[12] A contention of that nature is addressed in *United States* v. *Noland*, No. 95-323, which is set for argument in tandem with this case.

priority, its treatment is thus entirely dependent on whether the claim is to be subordinated under the "principles of equitable subordination" in Section 510(c) of the Bankruptcy Code.

Respondents nonetheless attempt to raise several new arguments at this late stage of the case—arguments that have nothing to do with equitable subordination or with the question presented on the writ of certiorari. Respondents claim that it was unnecessary for the courts below to rely on the "principles of equitable subordination" under Section 510(c) to subordinate the government's claim (although respondents asked them to) because, under respondents' new arguments, subordination of the government's claim would be permitted under other provisions of the Bankruptcy Code (Resp. Br. 40-44).[13]

[13] Respondents state (Resp. Br. 42) that Section 1122(a) of the Bankruptcy Code requires that the Section 4971(a) claim be classified separately from other general unsecured claims because it is not "substantially similar" to such claims. See 11 U.S.C. 1122(a). They assert that general unsecured claims "represent a pecuniary loss" while the Section 4971(a) claim does not. But the presence or absence of "pecuniary loss" does not distinguish the Section 4971(a) claim from other general unsecured claims. For example, the expectancy component of a claim for damages for breach of contract (as contrasted with a recovery of out-of-pocket losses) is also not a pecuniary loss resulting from an extension of credit, but it has not been suggested that judgments for such damages are not "substantially similar" to other unsecured claims. The requirement that claims in the same class be "substantially similar" relates to more basic considerations, such as as placing secured claims, priority claims and unsecured claims in different classes. See 5 *Collier on Bankruptcy* ¶ 1122.03, at 1122-8 (15th ed. 1995).

Respondents also raise the new contention (Resp. Br. 40-41) that subordination of the Section 4971(a) claim is permitted

The contentions that respondents now seek to raise were not raised in the bankruptcy court or the district court and, although at least some of them

by Section 1129(a)(7) of the Bankruptcy Code, 11 U.S.C. 1129(a)(7). That Section requires the bankruptcy court to find that *non*assenting claimholders will fare at least as well under the reorganization plan as they would in a liquidation under Chapter 7 of the Bankruptcy Code. See 11 U.S.C. 1129(a)(7)(i), (ii). Since nonpecuniary loss penalty claims are automatically subordinated in Chapter 7 cases (11 U.S.C. 726(a)(4)), respondents assert that they had a right to insist that, if the Section 4971(a) excise tax is not a priority claim, it be subordinated to the claims of competing general unsecured creditors in this Chapter 11 reorganization. That interpretation of Section 1129(a)(7) has been rejected in numerous cases. See, *e.g.*, *In re Virtual Network Services Corp.*, 98 B.R. 343, 344 (N.D. Ill. 1989), aff'd on other grounds, 902 F.2d 1246 (7th Cir. 1990); *In re A.H. Robins Co.*, 89 B.R. 555, 560 (E.D. Va. 1988). But even if respondents' interpretation of Section 1129(a)(7) were correct, the statute would nonetheless be irrelevant to this case because respondents did *not* dissent from the plan (instead, they proposed it), and the plan as confirmed provides for treatment of the Section 4971(a) claim as a general unsecured claim (i) if the Section 4971(a) claim is not a priority claim and (ii) if that claim is not subject to equitable subordination under Section 510(c). See page 14, *supra*. Whatever effect Section 1129(a)(7) may have, it expressly does not apply to creditors that have "accepted the plan" (11 U.S.C. 1129(a)(7)(i)). If the holder of an impaired claim does not dissent from the plan on this basis, it therefore cannot thereafter attack it on this basis.

There are numerous reasons why a creditor would not dissent from a plan that leads to a reorganization under Chapter 11 rather than a liquidation under Chapter 7. Section 1129(a)(7) does not require creditors to insist upon Chapter 7 liquidation if they choose instead to assent to a Chapter 11 plan.

were raised in the court of appeals, were not addressed by that court.[14]

The courts below confirmed respondents' plan solely on the premise that the Section 4971(a) claim is to be subordinated to general unsecured claims "under principles of equitable subordination" (Pet. App. 18a, 21a). Because the new contentions that respondents advance in this Court were not raised in, addressed by, or resolved by the courts below, and are not within the scope of the question presented in the writ of certiorari, they are not properly before the Court. See, *e.g.*, *Yee* v. *Escondido*, 503 U.S. 519, 533 (1992); *Youakim* v. *Miller*, 425 U.S. 231, 234 (1976)

[14] Respondents contend that there is no statutory "category" of claims that encompasses general unsecured claims and that courts therefore need not rely on "principles of equitable subordination" to treat claims within that group differently (Resp. Br. 42). But "[t]he general rule * * * is that 'all creditors of equal rank with claims against the same property should be placed in the same class.'" *Granada Wines, Inc.* v. *New England Teamsters and Trucking Industry Pension Fund*, 748 F.2d 42, 46 (1st Cir. 1984) (citations omitted). Each unsecured nonpriority claim therefore "should be treated like any other unsecured claim" (*id.* at 47). See *In re Los Angeles Land and Investments, Ltd.*, 282 F. Supp. 448, 454 (D. Haw. 1968), citing 6A *Collier on Bankruptcy* § 9.13(1), at 238 (14th ed. 1940); *In re Barney & Carey Co.*, 170 B.R. 17, 22 (Bankr. D. Mass. 1994). But see *In re U.S. Truck Co.*, 800 F.2d 581, 587 (6th Cir. 1986).

As this Court has explained, the principle of "[e]quality of distribution among creditors" is that "creditors of equal priority should receive pro rata shares" (*Begier* v. *IRS*, 496 U.S. 53, 58 (1990)). A court is not to "set up a subclassification of claims within a class given equal priority * * * and fix an order of priority for the sub-classes according to its theory of equity." *In re Columbia Ribbon Co.*, 117 F.2d 999, 1002 (3d Cir. 1941).

("Ordinarily, this Court does not decide questions not raised or resolved in the lower court.").

b. Turning at last to the contentions that *were* raised and addressed below, respondents argue that the decisions of this Court do not expressly require creditor misconduct as a prerequisite to application of the doctrine of equitable subordination (Resp. Br. 44-48).[15] As this Court summarized in *Comstock* v. *Group of Institutional Investors*, 335 U.S. 211 (1948), however, the doctrine of equitable subordination serves the narrow function of punishing creditors who engage in inequitable misconduct, by "depriv[ing] the wrongdoer of the fruits of his wrong." *Id.* at 229. It is undisputed that "there [has] been no inequitable conduct on the part of the [United States]" in this case (Pet. App. 6a). The doctrine of equitable subordination therefore simply does not apply.

[15] Respondents claim (Resp. Br. 44, 47, 48) that Section 502(j) of the Bankruptcy Code justifies subordination of a claim solely because of the "equities" of the case. That contention is not correct. Section 502(j) is a means of obtaining relief from a prior determination of the status of a claim when "the equities of the case" justify *reconsideration*. See 11 U.S.C. 502(j). Section 502(j) simply allows a court to reconsider the allowance or disallowance of a claim if reconsideration would be appropriate. See 3 *Collier on Bankruptcy* ¶ 502.10, at 502-107 to 507-108 (15th ed. 1995). Motions for reconsideration under Section 502(j) are analogous to motions under Federal Rules of Bankruptcy Procedure 9023 and 9024, which make Rules 59 and 60 of the Federal Rules of Civil Procedure applicable in bankruptcy cases. See *Colley* v. *National Bank*, 814 F.2d 1008, 1010 (5th Cir.), cert. denied, 484 U.S. 898 (1987); *S.G. Wilson Co.* v. *Cleanmaster Industries, Inc.*, 106 B.R. 628, 630 (Bankr. 9th Cir. 1989); *In re Stoecker*, 151 B.R. 989, 1001 (Bankr. N.D. Ill. 1993).

As we explain in detail in our opening brief in this case (Pet. Br. 21-30)—and in the opening and reply briefs in *United States* v. *Noland*, No. 95-323, which is being argued in tandem with this case—the requirement of creditor misconduct was a well established principle of equitable subordination when Congress codified those principles in Section 510(c) of the current Bankruptcy Code.[16] Respondents claim, however, that a different understanding of the statute is compelled by the statement of Representative Edwards that, "under existing law, a claim is generally subordinated only if [the] holder of such claim is guilty of inequitable conduct, or the claim itself is of a status susceptible to subordination, such as a penalty." 124 Cong. Rec. 32,398 (1978).

As a description of "existing law," the floor statement is simply incorrect, a fact that is confirmed by respondents' failure to identify a single case in which penalties were subordinated prior to enactment of the Bankruptcy Code in 1978.[17] Any misdescription of

[16] Respondents erroneously imply (Resp. Br. 45 n.31) that *In re Stirling Homex Corp.*, 579 F.2d 206 (2d Cir. 1978), and *In re Four Seasons Nursing Ctrs. of America, Inc.*, 472 F.2d 747 (10th Cir. 1973), represent pre-Bankruptcy Code applications of principles of equitable subordination in the absence of creditor misconduct. Neither case is an example of equitable subordination. Instead, both are examples of the fundamental bankruptcy rule that the claims of creditors are to be paid ahead of the interests of shareholders. See Pet. Br. 26-28 in *United States* v. *Noland*, No. 95-323. See also 472 F.2d at 749-750.

[17] As we describe in detail in our reply brief in *United States* v. *Noland*, No. 95-323 (at 5 n.2), prepetition nonpecuniary-loss penalty claims were disallowed prior to enactment of the Bankruptcy Code (see 11 U.S.C. 93(j) (1976)). Post-petition penalties were then, as now, given first priority (*Nicolas* v. *United States*, 384 U.S. 678, 694-695 (1966)). But no penalties

"existing case law" in the 1978 floor statement of Representative Edwards obviously does not alter the preexisting "principles of equitable subordination" that are to be applied under Section 510(c). *Burden* v. *United States*, 917 F.2d 115, 123 (3d Cir. 1990) (Alito, J., concurring in part and dissenting in part). Moreover, the Senate Report on the provision that was enacted as Section 510(c) accurately described its effect (S. Rep. No. 989, 95th Cong., 2d Sess. 74 (1978) (emphasis added)):

> "[A]ny subordination under this provision must be based on principles of equitable subordination. These principles are defined by case law, and have generally indicated that *a claim may normally be subordinated only if its holder is guilty of misconduct.*

The doctrine of equitable subordination permits courts to punish misconduct; it does not permit courts to alter the priorities that Congress established for innocent claimants. It therefore does not permit subordination of the innocent claim of the United States to the claims of other unsecured general creditors in this case.

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were subject to subordination (in the absence of creditor misconduct) under the judge-made "principles of equitable subordination" that Congress codified as Section 510(c) of the Bankruptcy Code.

For the foregoing reasons and the reasons set forth in our opening brief, the judgment of the court of appeals should be reversed.

Respectfully submitted.

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